

Testimony of
David L. Goldwyn
Assistant Secretary for International Affairs
U.S. Department of Energy
before the
Subcommittee on International Economic Policy, Export and Trade Promotion
The Senate Committee on Foreign Relations
April 12, 2000

MR. CHAIRMAN AND MEMBERS OF THE SUBCOMMITTEE:

I am pleased to appear before you today. I am also pleased to appear on this panel with Amb. John Wolf, with whom our Department works very closely on issues related to Caspian energy development. Amb. Wolf has outlined the Administration's Caspian policy and presented an up-to-date status report of the specific pipeline projects. Thank you for giving me the opportunity to address U.S. Caspian policy in an energy security, energy diversity and energy policy context.

U.S. Energy Interests in the Caspian

In support of the Administration's overall policy of promoting Caspian energy production and exports, the Department of Energy has pursued the following broad objectives:

- C Ensuring global energy security in a way that adequately addresses the strategic and economic interests of the United States as well as those of our allies and regional partners;

- C Promote the economic development of the countries in the region;
- C Promoting energy sector reform in the Caspian countries to attract foreign investment, thereby fostering regional prosperity and stability;
- C Supporting U.S. companies in their efforts to speed development of the region's energy resources;
- C Fostering viable and reliable alternatives for energy export; and
- C Ensuring energy development occurs in an environmentally responsible manner.

U.S. policy in the Caspian is both supported by and embodied in the Administration's National energy strategy which establishes clear, measurable objectives to help ensure that Americans will have affordable, clean and secure energy supplies into the 21st century. The goals of our energy strategy are to: 1) improve the efficiency of the overall energy system; 2) ensure against energy supply disruptions; 3) promote energy production and use in ways that respect our health and environmental values; 4) expand future energy choices, and 5) seek international cooperation of global energy issues.

Energy policy in the Caspian region specifically addresses these goals. Our Caspian policy reflects our view that the development of diverse, stable and reliable sources of energy is important to our national security and to the global economy. We can help ensure against national or international supply disruptions by diversifying sources of supply.

International cooperation and collaboration to increase and diversify world supply is crucial. The Energy Information Administration (EIA) expects world oil consumption to grow by an average annual rate of nearly two percent, reaching almost 84 million barrels in 2005 and over 103 million barrels a day in the year 2015. By the year 2015, the world's energy consumption is expected to be

48 percent higher than it was in 1995. The intense competition for scarce energy resources dictates the need for high levels of international cooperation to meet the world's energy demands through stable, market-driven means.

Under Secretary Richardson's leadership, we have taken several steps to strengthen domestic production and improve America's energy security for the long term. We have also been working to diversify world oil supplies so we're not dependent exclusively on any one region. Our efforts have focused on maintaining strong relationships with the major oil and gas producing nations, and encouraging their continued movement toward open markets, privatization and regulatory reform; promoting the development of new sources of supply and the infrastructure to support them -- in the Caspian, in Africa and in Latin America ; and promoting regional integration and infrastructure linkages.

There's concrete evidence that this approach is working. Since 1974, U.S. petroleum consumption has increased 16.4% while the economy has grown nearly 110%. Our top supplier of oil varies from week to week among Canada, Venezuela, Saudi Arabia and Mexico. We are less dependent on OPEC oil, and last year imported crude oil from 40 different countries.

How Important of a Resource Base is the Caspian?

Moving Caspian energy supplies into the global market figures prominently in our national security equation. While estimates of the size of regional oil and gas reserves vary widely, most observers consider that its resources will be on the same order of magnitude as those of the North Sea. Proven reserves in the Caspian region are estimated at 16 to 32 billion barrels of oil, which are comparable to North Sea reserves. It is possible that 186 billion additional barrels, roughly equivalent to more than a quarter of the Middle East's reserves, remain to be discovered.

We believe developing these resources and facilitating their delivery to world markets will help make energy markets more competitive, transparent and market-sensitive, three prerequisites of an efficient and smoothly functioning world energy sector.

How much the Caspian region actually produces and when it reaches peak production depends upon a number of factors. For illustrative purposes, it took 25 years for oil production in the North Sea to reach 6 million barrels per day under favorable circumstances. In the Caspian region, circumstances are less favorable. The region lacks supporting industries and infrastructure, and there is a shortage of drilling rigs. If investments continue in the Caspian region at the current pace, and if sufficient export outlets are developed, the Energy Information Agency's (EIA) "high" non-OPEC supply case scenario projects annual oil production to reach 4.2 million barrels a day by 2010. In the "low" non-OPEC supply case scenario, which assumes some project delays, oil production would reach 2.5 million b/d by 2010. These figures mean that at best the Caspian region will account for about 4.5% of total world oil supply in 2010. Nevertheless, this represents *almost one-half of new non-OPEC supply*. By way of comparison, in recent years Middle East-OPEC has supplied over 30% of total world oil consumption, and could supply 40% by 2020. The Caspian region will never replace the Middle East as a primary source of supply, but it will limit the extent of the growth of world oil and gas dependence on the Middle East. Thus, development of Caspian energy resources at the margin will play an important role.

Ensuring a Commercial Stake and Supporting U.S. Investments

We continue to support worldwide trade and investments by U.S. energy companies; such investments are key to unlocking Caspian energy resources and will have a corresponding benefit of

promoting regional stability and prosperity, as well as contributing to our nation's economy. U.S. technology is unrivaled and our companies employ the world's highest environmental protection practices and technologies. Their involvement will help ensure that development in the Caspian region achieves a desirable balance between maximizing production and environmental stewardship.

A fundamental thrust of our policy also relates to commerciality. That is, while we recognize the influence regional politics will play on the development of export routes, we have always maintained that commercial considerations first and foremost will determine the outcome. These massive infrastructure projects must be commercially competitive before the private sector and the international community will move forward. Our support of specific pipelines such as the Baku-Tbilisi-Ceyhan oil pipeline and trans-Caspian gas pipeline is not driven by a desire to intervene in private, commercial decisions. Rather, it derives from our belief that it is not in the commercial interests of companies operating in the Caspian states – nor in the strategic interest of the host states – to rely on a single, major competitor for transit rights. Since 1995, multinational oil companies have entered into joint arrangements to explore and produce the Caspian region resources, resulting in potential capital expenditures of up to \$90 billion. To date, multinationals have actually spent anywhere from \$5 billion to \$10 billion in developing these projects. To protect these investments, we must take a sensible, long-term view of the region's development, oil demand, and price trends in the oil market. Many (actually most) of the U.S. major oil and gas firms and engineering and construction firms have invested large sums of capital in huge offshore projects in the Caspian region. There will also be increased opportunities for American independents to invest in rehabilitating and redeveloping onshore oilfields. Feasibility studies, engineering, design, construction, and financing combine to make a protracted

process. With this huge investment exposure, planning now for long-term export and domestic distribution of the region's oil and gas is only prudent. That's one reason we are so aggressive in urging these countries to forge ahead now on infrastructure development in order to plan for the future.

Fostering Regional Cooperation and Energy Development

The development of multiple pipelines and diversified infrastructure networks to transport Caspian oil and gas resources will have the additional benefit of fostering the regional cooperation needed for peace and stability. Construction of oil and gas pipelines in an "east-west energy corridor" will serve to bind all of the countries together. The development of the region's energy resources creates opportunities for these countries to cooperate in new ways for the benefit of all. The speed and depth of that regional cooperation will have a direct effect upon the future economic prosperity of the individual countries.

Role of Russia

Russia has had a long and important role in Central Asia and the Caspian. Russia remains an important influence in the area since Russia is still the largest trading partner for each nation, Russia is a littoral state of the Caspian Sea, and Russia has the principal transportation routes for oil and gas out of the region.

In fact, until the recent opening of an "early oil" pipeline from Baku, Azerbaijan to Supsa, Georgia, Russia provided the only pipeline transportation out of the region and most of the rail transportation from the region. Kazakhstan and Turkmenistan currently ship oil through Russia, and Azerbaijan is expected to resume shipments through Russia soon. Moreover, in 2001, Kazakhstani exports are expected to begin flowing through the Caspian Pipeline Consortium (or CPC) pipeline to

the Russian Black Sea port of Novorossiysk. CPC, which includes both U.S. and Russian companies, will be an important new pipeline system. We strongly support it.

Most recently, Lukoil, the largest Russian oil company, has found a significant deposit of oil and gas in the Russian sector of the Caspian. As more wells are drilled over the next couple of years, the extent of this discovery will become clearer. If commercially viable, this oil could be used either in local refineries, or shipped in the CPC, since Lukoil has a small interest in the CPC.

The U.S. always has viewed Russia as an important partner in the development of oil and gas resources in the Caspian and has encouraged Russia to participate in the development of multiple transport routes from the region. As a littoral state, Russia has made its voice known regarding how resources should be developed in the Caspian Sea in an environmentally sound manner. Since the Caspian is an important fishery for Russia, use of the Caspian for transportation either across it or under it, can have an economic impact on Russia. As a result, its views are important to the overall development of the hydrocarbon resources around or in the Caspian Sea. We look forward to the continuation of our work with the new government in Russia to develop economic, environmentally sound transportation alternatives through and from the Caspian region.

Role of Turkey

We want to assist our European ally, Turkey, in strengthening its energy security and meet its development goals. Just two weeks ago, I had the privilege of leading the 8th session of U.S.-Turkey energy consultations. This interagency effort was established to discuss Turkey's strategy for moving forward with development of its energy sector, meeting the growing demand for electricity, diversifying its gas supplies, developing alternative fuels to diversify energy sources, and identifying further steps for

development and construction of oil and gas pipelines through Turkey for Caspian resources.

In this regard, we share Turkey's environmental concerns about the potential increase in traffic through the Bosphorus. Further, we do not want to see the Bosphorus become a potential choke point for a significant share of the world's oil supplies, which would heighten environmental concerns and possibly impede the development of Caspian energy. One of the strengths of the Baku-Tbilisi-Ceyhan route we support is that it would provide an alternative to increased flows of oil through the Bosphorus.

Development of natural gas pipelines is also important to the countries in the region. Turkey currently has gas shortages and plans to increase its gas imports more than five-fold by 2010. Potential alternatives to reliance on Russia or Iran include purchases of gas from Turkmenistan and Azerbaijan.

Intensifying our Engagement with Regional Governments

One of the more visible ways we are implementing our Caspian policy involves the engagement of Cabinet-level and senior-level visits to the region, and the establishment of formal government-to-government dialogues. For example, Secretary Richardson has traveled to Caspian capitols three times, most recently last November with President Clinton to take part in signing agreements on Baku-Tbilisi-Ceyhan and the trans-Caspian Gas Pipeline.

As the countries in the region develop their political systems, new governmental structures and new legal frameworks, they will constantly struggle to achieve sometimes conflicting goals. They will have to formulate and implement domestic policies that create an investment friendly environment. This is not always an easy task, because as you are all keenly aware, there is sometimes tension between political and economic realities. As we establish a sound basis for trust with these countries, it will be our role to share our best advice based on our own experiences with energy development, to work

with them to identify international resources, and to work in partnership with U.S. industry to resolve problems that will inevitably arise.

At the Department of Energy, we have established a dialogue with the countries of the region on issues such as climate change, energy efficiency and conservation, and environmentally sustainable energy development. We are working with them on policy issues such as energy sector liberalization and energy regulation, and establishing policies that support balance in energy development. And we are looking for new areas where we can be helpful, including developing a regional system for oil spill response. This cooperation is an integral part of our efforts to establish a positive relationship with the countries of the region that will contribute to regional development, political stability, and healthy and growing trade linkages.

The Caspian countries continue to reach out to the U.S. and to foreign investment. We are working to maintain the momentum behind our support for these governments and the private sector. We welcome an ongoing dialogue with Congress on Caspian energy development. We have followed with interest the numerous Congressional delegations that have traveled to the region. We will forward to working with you in meeting the many challenges ahead.